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SIPDIS

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SUBJECT: NEW ERA IN TURKISH RUSSIAN ECONOMIC RELATIONS? --

NOT

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Sensitive But Unclassified.

¶11. (SBU) Summary: The December 5-6 visit of Russian President Putin to Turkey was portrayed by Turkish politicians and the press as a turning point in Russian-Turkish relations. Putin and Turkish President Sezer asserted that the rapid growth of bilateral trade is leading to an emerging "Multidimensional Partnership" with the economic relationship at the forefront. However, the visit failed to meet expectations as few of the ambitious economic initiatives agreed to at the Turkey-Russia Joint Economic Commission (JEC) meeting the week before were endorsed during the Putin visit. A broad energy MOU was short on clear commitments and left all Bosphorus shipping and bypass issues still in play. In the end, little was accomplished to improve an economic relationship with lots of promise, but many problems. (Septel reports the political context of the Putin visit.) End Summary.

Trade Boom

¶12. (SBU) Vladimir Putin visited Ankara December 5-6, marking the first visit of a Russian President to Turkey. The visit followed a meeting a week earlier of the Russia-Turkey Joint Economic Commission in Moscow, the first in four years, and demonstrated the desire of both sides to take advantage of growing bilateral trade to broaden bilateral economic cooperation. Russia is Turkey's second largest trading partner after Germany. This year, two-way trade volume is expected to exceed \$10 billion, a dramatic increase from \$200 million in 1989 and \$6.7 billion in 2003. However, most of that is accounted for by Russian natural gas, oil and refined product sales, resulting in a large bilateral trade deficit for Turkey. (In the first 10 months of 2004, Turkey has imported \$6.9 billion while exporting only \$1.5 billion, for a deficit of \$5.4 billion). Turkish officials pressed Russian officials to balance the trade, specifically by implementing a Soviet-era offset agreement for natural gas purchases. Turkish MFA officials noted the Russian assertion that the bilateral trade deficit is largely offset by the estimated 1.7 million Russian tourists spending about \$1 billion at Turkish resorts, Turkish construction contracts of about \$2 billion and an estimated \$2-3 billion of annual undocumented "suitcase trade" from Turkey to Russia.

An Ambitious Agenda . . .

¶13. (SBU) Prior to the visit, Turkish officials expressed their high aspirations for trade with Russia. Foreign Trade Minister Tuzmen, who led the Turkish delegation at the JEC, said Turkey expects bilateral trade to reach \$25 billion by 2007, which would make Russia Turkey's number one trade partner. Turkish officials said the goal for the JEC was to build a modern structure for the bilateral economic relations so that trade and investment can flourish. Some of the steps agreed to were practical, such as an investment protection agreement, while others, like the attempt to enforce an offset agreement for natural gas sales, are unlikely to go anywhere.

¶14. (SBU) The Joint Economic Commission agreed to pursue a long list of initiatives:

- rewrite the 1937 bilateral trade agreement.
- examine the possibility of establishing a free trade agreement with Russia, especially if Turkey does not achieve full EU membership.
- agreed to Russian regulation of undocumented suitcase trade. Turkey fears that Russian restrictions will drastically reduce this important income source for Turkey's low-income northeast and asked for a transition period to delay implementation.
- eliminate non-tariff barriers, such as the Russian imposition of a high reference price on Turkish industrial goods.
- draft new agreements on double taxation and investment protection.
- establish a consultative mechanism to address a long list of investment disputes. Turkish officials are increasingly frustrated by the problems their companies face doing

business in Russia.

- implement the offset agreement for natural gas purchases. The 1984 agreement to sell Soviet gas to Turkey included a provision guaranteeing Soviet purchases of Turkish goods equal to 70% of the natural gas sold. The offset agreement functioned somewhat until the early 1990s. In Moscow, the Russians acknowledged that the offset clause remained valid but agreed only to talk about ways to implement it.
- create an tax-free zone for Turkish companies in Moscow.
- resolve Russia's debt to Turkey's EXIM Bank.
- reduce Russian trade barriers to Turkish food exports (especially chicken).
- draft a civ air agreement.

15. (SBU) Investments and Energy: Putin brought with him to Ankara a long list of investment proposals totaling \$20 billion. The list includes Russia's interest in Turkey's privatization of the natural gas distribution network, electricity generation facilities and the Seydisehir Aluminum plant (see reftel). Russian officials also mentioned grand plans for 1) extending the Blue Stream gas pipeline to the Mediterranean port of Ceyhan and construction of an LNG facility to export Russian gas to Israel; 2) selling Russian electricity to Turkey via Georgia; and 3) a railway/ferry network connecting Turkey and Russia directly. In a joint statement on energy, the Turks and Russians announced plans to cooperate on nuclear power (septel); endorsed Gazprom's desire to invest in a range of natural gas projects in Turkey; and welcomed Russian investment in the electricity sector. Although the high court recently canceled the tender for the TUPRAS refinery company, won by a consortium led by Russian firm Tatneft, a Turkish MFA official confirmed press reports that PM Erdogan promised that the tender would be reopened with favorable consideration to Tatneft.

16. (SBU) Bosphorus: Both sides expressed commitment to achieving a Bosphorus bypass solution and discussed the merits of the various options. The Turkish side emphasized environmental sustainability (in support of Samsun-Ceyhan, and in opposition to trans Thrace and Burgos-Alexandropoulos) and the Russian side emphasized economic feasibility. While the press reported extensively that the Russians were abandoning their previous support of a trans-Thrace bypass route to support the Turkey favored Samsun-Ceyhan route, Embassy contacts stated that no firm agreement on Samsun-Ceyhan had been reached. Acknowledging that Bosphorus tanker shipping had limits and was dangerously congested, the Russians offered assistance on shipping safety from their Baltic experience. The Turks expressed confidence in their own expertise and new Vessel Traffic System (VTS). Russian Oil Minister Khristenko said making a bypass pipeline economically feasible would require "preferential treatment" from the sponsoring country. According to the MFA, their proposal for "Voluntary Principles" for public/private partnership on working together on achieving a Bosphorus bypass solution was presented to the Russians.

. . . But Little to Show

17. (SBU) Putin and Sezer endorsed the ambitions of both countries to boost bilateral economic ties. "Economic cooperation usually falls behind political interaction between Russia and its partners, Putin said, but in the case of Turkey this is vice versa." The two signed a joint declaration on economic ties and a series of specific agreements on energy cooperation, IPR for defense items, and prevention of accidents in the Black Sea. It is notable, however, that few of the ambitious projects agreed to in the JEC were endorsed during Putin's visit, and the other big economic issues, like agreement on a Bosphorus Bypass pipeline, did not succeed. In the end, we suspect, most of the ambitious projects will end up as nothing more than words on paper. Confirming that view, just days after the visit, the mood of the Turkish press darkened, with one paper reporting that "the historical opportunity for making a breakthrough in ties with Russia that emerged with the visit of Russian President Vladimir Putin to Turkey had been missed."

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